

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to  
Review Policies Concerning  
Intrastate Carrier Access Charges

Rulemaking 03-08-018  
(Filed August 21, 2003)

**REPLY COMMENTS OF THE UTILITY REFORM NETWORK AND  
THE DIVISION OF RATEPAYER ADVOCATES  
ON THE REVISED BUSHEY DRAFT DECISION  
AND THE PEEVEY ALTERNATE DRAFT DECISION**

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## CERTIFICATE OF SERVICE

## **I. INTRODUCTION**

Pursuant to Rule 77.3 of the Commission's Rules of Practice and Procedure, and the March 14, 2006 Notice of Availability, The Utility Reform Network (TURN) and the Division of Ratepayer Advocates (DRA)<sup>1</sup> submit these Reply Comments on the Revised Bushey Draft Decision's (Bushey RDD)<sup>2</sup> and the Peevey Alternate Draft Decision (Peevey ADD).<sup>3</sup> TURN and DRA (TURN/DRA) respond to the Comments on the Bushey RDD and the Peevey ADD filed by several parties on April 3, 2006. TURN/DRA support the Comments of CALTEL and CCTA, but find significant problems with several recommendations of SBC and Verizon.<sup>4</sup> Notwithstanding TURN/DRA's continued opposition to the principle of revenue neutrality in this case, TURN/DRA continue to urge the Commission to adopt the Bushey RDD with the modifications discussed herein and in our 4/3/06 Comments.<sup>5</sup>

## **II. THE SURCHARGE SHOULD NOT INCLUDE LOST REVENUES RELATED TO ILEC AFFILIATES**

In opposing the Bushey RDD, specifically the provision excluding revenues associated with ILEC-affiliated interexchange carriers (IXCs), SBC and Verizon argue that the exclusion of intra-LEC revenues violates the "revenue neutrality" adopted in Phase I of this proceeding. These arguments distract from the reality of today's telecommunications market, including the mergers of SBC with AT&T, and of Verizon with MCI. They also

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<sup>1</sup> The Office of Ratepayer Advocates (ORA) returned to being designated as the Division of Ratepayer Advocates (DRA) as of January 1, 2006.

<sup>2</sup> Revised Draft Decision of ALJ Bushey, "Final Opinion Modifying Intrastate Access Charges and Creating Memorandum Account" (mailed 3/14/2006) (Bushey RDD).

<sup>3</sup> Alternate Draft Decision of President Peevey, "Final Opinion Modifying Intrastate Access Charges and Creating Memorandum Account" (mailed 3/14/2006) (Peevey ADD).

<sup>4</sup> Opening Comments of the California Association of Competitive Telephone Companies on Revised Draft Decision of ALJ Bushey and the Alternate Decision of President Peevey (April 3, 2006 (CALTEL Comments); Comments of the California Cable and Telecommunications Association on the Assigned Administrative Law Judge's Revised Draft Decision and the Assigned Commissioner's Alternate Draft (April 3, 2006) (CCTA Comments); Comments of Pacific Bell Telephone Company (U 1001 C) on the Revised Draft Decision of Administrative Law Judge Bushey (April 3, 2006) (SBC Comments on Bushey RDD); Comments of Pacific Bell Telephone Company (U 1001 C) on the Alternate Draft Decision of President Peevey (April 3, 2006) (SBC Comments on Peevey ADD); Opening Comments of Verizon California Inc. (U 1002 C) and Verizon West Coast Inc. (U 1020 C) on the Revised Draft Decision of ALJ Bushey and Alternate Decision of President Peevey (April 3, 2006) (Verizon Comments).

<sup>5</sup> Comments of The Utility Reform Network and the Division of Ratepayer Advocates on the Revised Bushey Draft Decision and the Peevey Alternate Draft Decision (April 3, 2006) (TURN/DRA Comments).

ignore the reason that the Commission opened this proceeding – because access charges priced above cost pose a threat to the competitiveness of the intrastate long distance market to the extent that the ILECs have affiliated IXCs competing with independent IXCs.

**A. Excluding Intra-LEC Access Revenues Is Consistent With The Very Premise Of This Proceeding**

In D.04-12-022, the Commission clearly identified anti-competitive potential of having above-cost access charges:

This Commission has so far rejected proposals by interexchange carriers to eliminate the NIC and TIC for intrastate rates. However, changes in the industry over the past 15 years motivate us to review these charges. For a while, the relationship between the cost of access and charges for access did not significantly affect the competitiveness of any particular carrier. Although high access charges might dampen innovation or investments in long distance markets, all carriers faced the same level of charges and none acquired any advantage due to access charge pricing structures. The potential impact of high access charges, however, changed after LECs entered long distance markets in 2002. To the extent access charges are set above cost, LECs have an opportunity to price long distance services at levels that are anti-competitive. In effect, LECs could collect high access charge revenues from competitors while charging very low retail toll rates. Even if LEC long distance services are offered through affiliates, excess profits from access charges may be passed along to the affiliate through the parent company.<sup>6</sup>

If the Commission has concluded that the NIC and TIC should be removed from the access charges of SBC and Verizon, it does not make sense to require ratepayers to make up the difference for the minutes associated with the IXCs of those very ILECs. Now that the vast majority of intrastate access minutes are for access services provided to ILEC affiliates, it is particularly nonsensical. If access charges are above-cost when the NIC and TIC elements are included (an implicit conclusion that the Commission appears to have reached), the surcharges collected from ratepayers represent, from the perspective of the ILECs' parent companies, excess revenues that can be used to undercut the long distance rates of independent IXCs, that can simply be retained as profits if there is insufficient

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<sup>6</sup> D.04-12-022, *mimeo*, at 6-7 (emphasis added).

competitive pressure to lower rates. And with their significantly greater market share post-merger, the affiliated IXC's now have a greater ability to exercise this option.

**B. Excluding Intra-LEC Access Charges Is Not Contrary To Revenue Neutrality**

TURN/DRA agree with the analysis of CCTA that, in excluding intra-LEC access charge revenues from the surcharge, the Bushey RDD “fulfills the requirement of D.04-12-022 by achieving revenue neutrality in a manner that is consistent with the way the policy has been defined in past decisions....”<sup>7</sup> As CCTA goes on to explain,

Just the opposite would result if the [Peevey ADD] were adopted. The ILECs would receive more revenues than they were receiving before the NIC and TIC were eliminated because they would receive actual dollars for what previously had been paper transactions. This is by definition a windfall that is contrary to [the] Commission’s policy on revenue neutrality. Along the same lines, its cumulative effect is far greater than zero. Finally, because it would result in an increase in revenues for the ILECs that they would not otherwise have access to, if anything, it mocks the principle of providing ILECs “fair opportunity” to earn a competitive rate-of-return by giving them access to revenues they would not have generated on their own absent the rate reduction.<sup>8</sup>

Thus, DRA and TURN support CCTA’s observation that the Peevey ADD defies the spirit of revenue neutrality as this Commission has historically interpreted it.

**C. Consistent With The Commission’s Merger Approvals, The Commission Should Consider The Vertically-Integrated Natures Of SBC And Verizon**

In light of the surcharges both draft decisions seek to impose on ratepayers, the Commission should be conservative in determining the amounts to be recovered through the surcharge. In this case, SBC and Verizon have just spent most of last year promoting the alleged consumer benefits of their mergers. One of the many aspects of the mergers between SBC and AT&T, and between Verizon and MCI, evaluated by both the Commission and the FCC was the vertical integration between local and long distance

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<sup>7</sup> CCTA Comments at 3.

<sup>8</sup> CCTA Comments at 4.

facilities.<sup>9</sup> The significance for this proceeding is that access charges – or the lack thereof – can play a valuable role in a merger involving vertical integration of a local and long distance company, as the Bushey RDD itself references.<sup>10</sup>

But in challenging the Bushey RDD, the ILECs attempt to carefully limit the scope of this Commission’s analysis. SBC and Verizon claim that access charges between local and long distance affiliates are more than mere “paper” transactions, essentially asking the Commission to view these transactions from only one perspective – that of the ILEC.<sup>11</sup> This proceeding was opened, however, due to concern about the rates customers face in the unregulated long distance market, naturally suggesting that the Commission should be concerned about how IXCs will react to the Commission’s resolution of this proceeding. If the Peevey ADD is adopted, it is clear how a parent company overseeing the vertical integration of a local and a long distance companies would view a surcharge that includes affiliate-related access services – as an opportunity to either lower long distance rates or, if low competitive pressures allow, retain additional profit. Accordingly, the Commission should acknowledge the realities of the current telecommunications market and treat access charges between an ILEC and its IXC affiliate, for the purposes of this proceeding, as “paper” transfers that should not be subsidized by ratepayers.

### **III. CLARIFICATIONS TO THE SURCHARGE METHODOLOGY**

The three parties that addressed the surcharge calculation and implementation methodology – TURN/DRA, Verizon, and SBC – agree that the methodology should be clarified, but propose different solutions.<sup>12</sup> While TURN/DRA support, or do not object to,

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<sup>9</sup> For example, the FCC concluded with regard to the SBC/AT&T merger: “We find that significant benefits are likely to result from the vertical integration of the largely complementary networks and facilities of SBC and AT&T. The Applicants assert that their networks are complementary, with SBC providing an extensive network with substantial local fiber, Cingular having an advanced and extensive wireless network, and AT&T providing a global fiber optic long distance network and global data capabilities.” *In the Matter of SBC Communications Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, WC Docket No. 05-65, *Memorandum Opinion and Order*, FCC 05-183 (rel. November 17, 2005) at para. 191. See also *In the Matter of Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, WC Docket No. 05-75, *Memorandum Opinion and Order*, FCC 05-184 (rel. November 17, 2005) at para. 203.

<sup>10</sup> Bushey RDD at 11, note 5.

<sup>11</sup> See SBC Comments on Bushey RDD at 5-7; Verizon Comments at 3-6.

<sup>12</sup> TURN/DRA Comments at 7-9; SBC Comments on Peevey ADD at 3; SBC Comments on Bushey RDD at 8-9; Verizon Comments at 8-9. Parties refer to the surcharge methodology in Appendix A of both the Bushey RDD and the  
(continued on next page)

some of the proposed changes, TURN/DRA are very concerned about the ILECs' proposal to apply the surcharge only to the "local" or "exchange" billing base.<sup>13</sup> As TURN/DRA explained in its Comments, this would effectively place a disproportionate burden on residential ratepayers.<sup>14</sup> The Commission should instead adopt a ratemaking method that more equitably spreads the revenue recovery across the three categories of local, toll, and access services, rather than solely to local services.<sup>15</sup> This would entail minor modifications to the proposed Findings of Fact (FOF) Conclusions of Law (COL), Ordering Paragraphs (OP), and Attachment A submitted by SBC and Verizon.<sup>16</sup>

SBC and Verizon recommend additional clarifications to the Bushey RDD and the Peevey ADD. For example, both ILECs recommend that surcharge assessment commence simultaneously with the Commission's elimination of the NIC/TIC.<sup>17</sup> TURN/DRA do not object to this. In addition, both SBC and Verizon explain that a billing base is a revenue amount, not a count of "minutes of use."<sup>18</sup> TURN/DRA agree.

#### **IV. CONCLUSION**

For the reasons identified herein, TURN and DRA urge that the revised Bushey Draft Decision be adopted, with the modifications discussed herein and in our 4/3/06 Comments.

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Peevey ADD (Appendix A).

<sup>13</sup> It is DRA's understanding that the terms "local" and "exchange" in this context are synonymous. SBC Comments on Peevey on ADD at 2; SBC Comments on Bushey RDD at 9; Verizon Comments at 8.

<sup>14</sup> TURN/DRA Comments at 9.

<sup>15</sup> *Id.* As TURN/DRA discussed in its Comments, the original Verizon rate design proposal (which was subsequently withdrawn) would be a reasonable way to accomplish this objective. *Id.*; Declaration of Dr. Robert T. Tanimura (Feb. 14, 2005) (Verizon Declaration) at 2-3. Verizon proposes to increase rates for: "1) business basic exchange, 2) former-Contel residential basic exchange service (to bring into parity with former-GTE rates), 3) remote call forwarding, 4) additional directory listings, 5) directory assistance, 6) coin sent paid operator handled surcharge, 7) business traffic study service, and 8) digital channel service." Verizon Declaration at 3.

<sup>16</sup> With regard to SBC's proposed modifications in Appendix 1 of its Comments, this would require the deletion of "exchange" in the following: COL 3; OP 3 and 5; for Attachment A, in Steps 1, 2, 3, and 4 under "Calculate the Surcharge" and in the last two sample tables. For the sample tables, "Exchange Billing Base" should be replaced with "Total Billing Base." With regard to Verizon's proposed modifications, the phrase "applied to the local billing base" should be deleted in FOF 4.

<sup>17</sup> SBC Comments on Peevey ADD at 2; SBC Comments on Bushey RDD at 9; Verizon Comments at 7-8.

<sup>18</sup> SBC Comments on Peevey ADD at 3; SBC Comments on Bushey RDD at 9.

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**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a copy of “**REPLY COMMENTS OF THE UTILITY REFORM NETWORK AND THE DIVISION OF RATEPAYER ADVOCATES ON THE REVISED BUSHEY DRAFT DECISION AND THE PEEVEY ALTERNATE DRAFT DECISION**” in **R.03-08-018** by using the following service:

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Executed on **April 10, 2006** at San Francisco, California.

/s/ Imelda Eusebio

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Imelda Eusebio

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